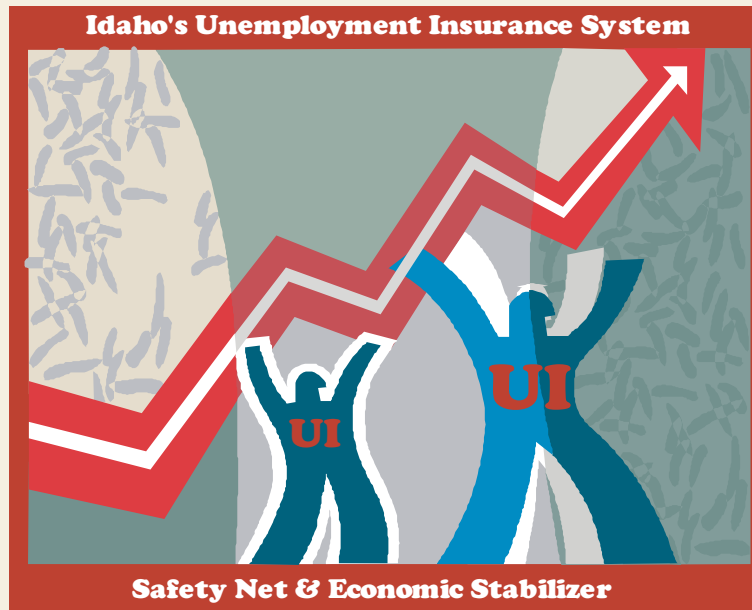


# Idaho Unemployment Insurance 2004 ~ Annual Year-End Brief

January 2005



The Unemployment Insurance Trust Fund system finances the insurable unemployment risk. The one overriding principle of building a trust fund to pay Unemployment Insurance (UI) benefits is that the fund reserves should be adequate during periods of economic health to pay benefits during periods of economic downturn.

*“Recessions would be about 15% deeper if the UI program did not exist. (US Dept. of Labor - 1999)”*

## # 1 UI Trust Fund and Solvency

Idaho's 2004 year-end UI Trust Fund balance is estimated to be approximately \$191 million - 11 percent less than the \$213 million recorded at the close of 2003.

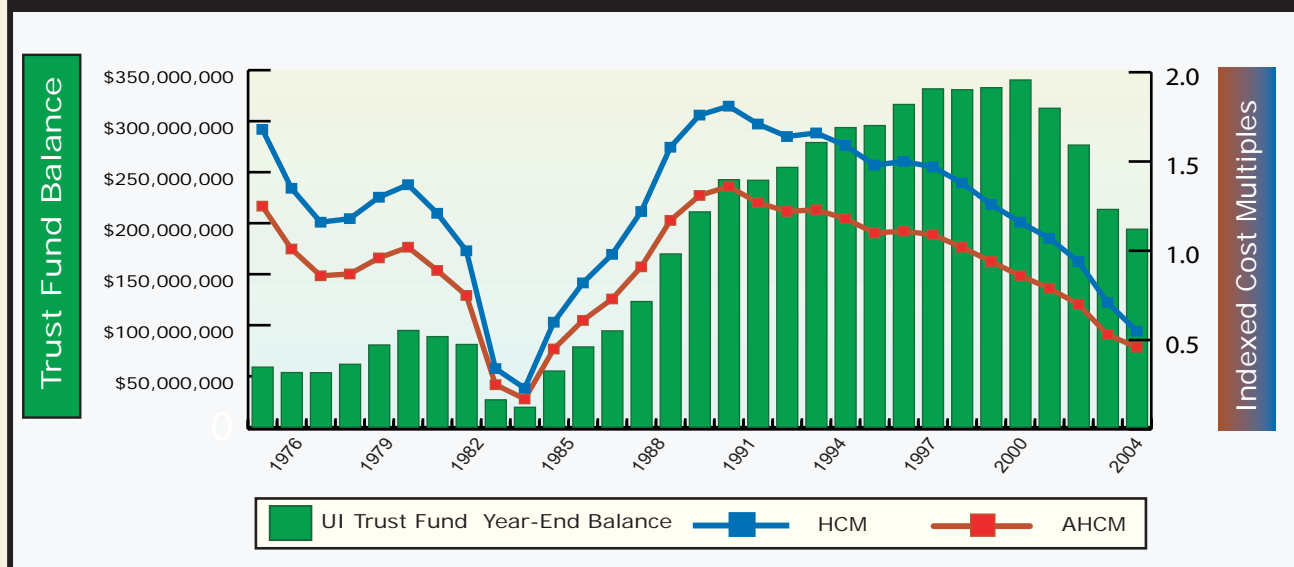
Fundamental question: ***What size should the UI Trust Fund reserves be to meet a potential drawdown from a recessionary economy?*** The absolute dollar balance of the UI Trust Fund has little value in determining the financial health of a trust fund since the liability to the fund is greater as Idaho's labor force and wages continue to grow. Therefore, the UI Trust Fund balance must be made relative to known values such as the High Cost Multiple (HCM), Average High Cost Multiple (AHCM), and the ratio of the fund to total wages to measure solvency.

### ~ Definitions ~

#### **Average High Cost Multiple (AHCM)**

Another relative 'rule-of-thumb' is the AHCM recommended by the U.S. Advisory Council on Unemployment Compensation: "Congress should establish an explicit goal to promote the forward funding of the Unemployment Insurance system. In particular, during periods of economic health, each state should be encouraged to accumulate reserves sufficient to pay at least one year of Unemployment Insurance benefits at levels comparable to its previous high cost. For purposes of establishing this forward-funding goal, the previous high cost should be defined as the average of the three highest annual levels of Unemployment Insurance benefits that a state has paid in any of the previous 20 calendar years."

**Idaho UI Trust Fund Year-End Balances with Indexed Cost Multiples**



Although the absolute levels of the UI Trust Fund have risen throughout the '90s, the adequacy indicators (AHCM & HCM) fell significantly during this same period. In fact, although today's UI Trust Fund is twice the size it was in the '70s, the trust fund is only half as adequate as measured by the AHCM and HCM. This is mostly due to Idaho's ever increasing labor force the fund is designed to support, as well as the recent tax relief provided by the tax freeze at schedule II.

#### **High Cost Multiple (HCM)**

The premise of the HCM is that each state should maintain a minimum trust fund balance which is 1½ times larger than the indexed amount of UI benefits paid out in 12 months during the worst case recession in recent history. The high cost multiple is derived by dividing the ratio of a state's year-end UI trust fund balance to total covered wages paid during the year by the state's high cost rate.

# UI Trust Fund Solvency

-Tax Freeze

-Taxes and Benefits

## FROZEN AT SCHEDULE II

In Idaho, the Legislature has frozen UI tax rates at schedule II since 2002 (see tax table below). While this legislation has resulted in considerable savings to employers, the UI Trust Fund has become more insolvent over that time period. Since taxes have been artificially frozen the infusion of tax dollars into the fund has been outpaced by the benefits paid to claimants from the trust fund. The tax schedule that is used for any given year is the major contributor to the effective tax rate. Tax rate schedule II was in effect in CY2001 and CY2002. Which tax schedule that is used is an outcome of Idaho's indexed tax rate formula, which also takes into consideration many other factors such as the size of trust fund, the size of total Idaho covered payroll, and average costs of benefits. However, this formula was not used in rate year 2002, 2003 and 2004 because the Idaho Legislature froze UI taxes at schedule II for those years.

### \*\*\*\* IDAHO UNEMPLOYMENT INSURANCE SYSTEM \*\*\*\* SCHEDULES OF TAXABLE WAGE RATES

Effective January 1, 1998

Tax Schedules		I	II	III	IV	V	VI	VII	VIII	IX		
Rate Classes	POS			Taxable Wage Rates for Eligible (Positive) Employers (Percent of TAXABLE wages)								
		1	0.1	0.2	0.4	0.8	1.2	1.6	2.0	2.2	2.4	
		2	0.2	0.4	0.6	1.0	1.4	1.8	2.2	2.4	2.6	
		3	0.4	0.6	0.8	1.2	1.6	2.0	2.4	2.6	2.8	
		4	0.6	0.8	1.0	1.4	1.8	2.2	2.6	2.8	3.0	
		5	0.8	1.0	1.2	1.6	2.0	2.4	2.8	3.0	3.2	
		6	1.0	1.2	1.4	1.8	2.2	2.6	3.0	3.2	3.4	
	7	1.2	1.4	1.6	2.0	2.4	2.8	3.2	3.4	3.6		
	STANDARD-RATED EMPLOYERS			Taxable Wage Rates for Standard--Rated Employers (Percent of TAXABLE wages)								
		1.3	1.5	1.7	2.1	2.5	2.9	3.3	3.5	3.7		
	NEG				Taxable Wage Rates for Deficit Employers (Percent of TAXABLE wages)							
		-1	2.4	2.6	2.8	3.2	3.6	4.0	4.4	4.6	4.8	
		-2	2.8	3.0	3.2	3.6	4.0	4.4	4.8	5.0	5.2	
		-3	3.2	3.4	3.6	4.0	4.4	4.8	5.2	5.4	5.6	
		-4	3.6	3.8	4.0	4.4	4.8	5.2	5.6	5.8	6.0	
		-5	4.0	4.2	4.4	4.8	5.2	5.6	6.0	6.2	6.4	
-6		5.4	5.4	5.4	5.4	5.6	6.0	6.4	6.6	6.8		
As a percent of "TAXABLE" wages ➡		1.00	1.19	1.39	1.79	2.19	2.59	2.99	3.19	3.39		
As a percent of "TOTAL" wages ➡ (Average Effective Tax Rate)		0.7	0.8	0.9	1.2	1.5	1.7	2.0	2.1	2.3		

## TAXES and BENEFITS

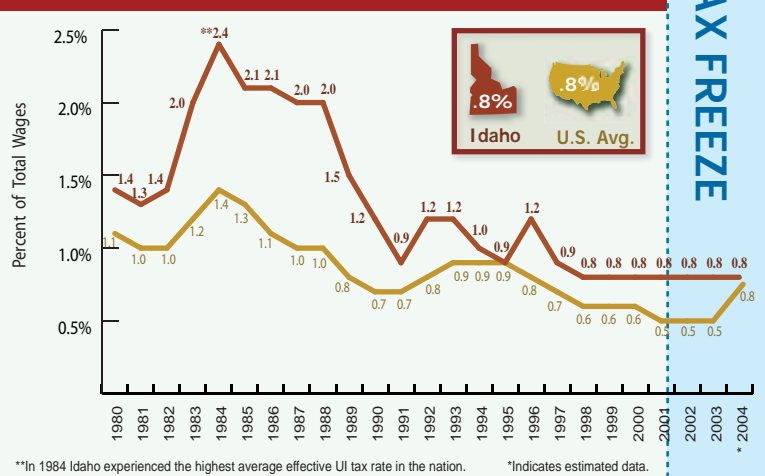
The first graphic depicts the average effective tax rate in Idaho since 1980. The second graphic on the next panel compares the taxes paid into the trust fund to the benefits paid out of the fund since 1980. During CY2004, approximately \$111 million in taxes were paid into the trust fund, while almost \$140 million was paid out in benefits, resulting in a 26 percent deficit. This annual deficit has closed from the 56 percent deficit that was recorded in 2003. Due to the current legislated tax freeze, the same rate schedule was in effect both years. Therefore the closing deficit is the result of the improving economy in 2004.

## TAX SAVINGS

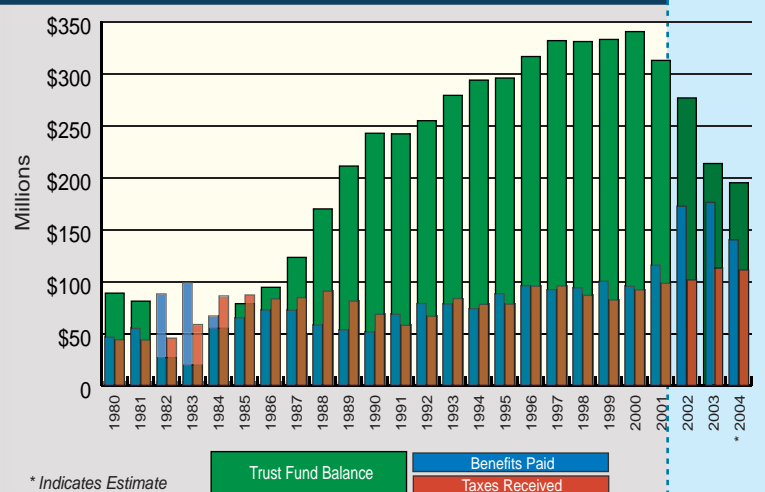
Overall the legislated tax freeze has saved employers more than \$110 million over the last three years. The graphic at the bottom of the following panel depicts the precipitous decline in the average effective tax rate over the last 20 years. In 1984 Idaho's effective tax rate was the highest in the nation, while in 2004 at 0.8% it was near the national average that is increasing to nearly 0.8%.

## Comparative Analyses of the Impact of Taxes and Benefits on the Unemployment Insurance Trust Fund

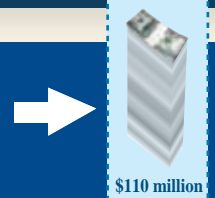
UI Average Effective Tax Rates (to Total Wages) 1980 to \*2004



Trust Fund Balance, Taxes Received, And Benefits Paid  
1980 - 2004



The result of UI taxes being frozen at schedule II has resulted in approximately \$110 million in tax savings to Idaho Employers.



## Definition ~ EFFECTIVE TAX RATE

The effective tax rate (see first chart this page) is the tax rate employers pay based upon total covered wages as opposed to the taxable wages discussed in a previous section. The effective tax rate is defined as taxes paid by employers divided by total covered wages. Its usefulness lies in the fact that valid comparisons can be made with other states, by industry and over periods of time. Most important is the fact that the effective tax rate makes allowances for differences in tax rate schedules, tax bases, and tax laws, and provides a common basis for evaluation.